STATE OF MICHIGAN

IN THE SUPREME COURT

NATIONAL WINE & SPIRITS, INC.,
NWS MICHIGAN, INC., and
NATIONAL WINE & SPIRITS, L.L.C.,

Plaintiff-Appellants

v

STATE OF MICHIGAN,

Defendant-Appellee

and

MICHIGAN BEER & WINE
WHOLESALERS ASSOCIATION,

Intervening Defendant-Appellee.

Supreme Court No. 126121

Court of Appeals
No. 243524

Circuit Court for the County of
Ingham No. 02-13-CZ

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PLAINTIFFS-APPELLANTS' SUPPLEMENTAL BRIEF

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INTRODUCTION

Just as they did in the case of *Granholm v Heald*, 544 US __; 125 S Ct 1885; 161 L Ed 2d 796 (2005), Defendant/Appellees State of Michigan ("State") and the Michigan Beer and Wine Wholesalers Association (the "Association", collectively referred to as "Defendants"), rely heavily on the argument that the twenty-first amendment to the United States Constitution gives the State the unfettered right to regulate every aspect of the alcoholic beverage trade, even if that regulation is protectionist and would otherwise violate the Commerce Clause of the Constitution. This argument was soundly rejected by the Supreme Court in *Granholm*, a case which struck down Michigan's prohibition of the direct shipment of out-of-state wines:

> Our more recent cases, furthermore, confirm that the Twenty-first Amendment does not supersede other provisions of the Constitution and, in particular, does not displace the rule that States may not give a discriminatory preference to their own producers.

Granholm, 125 S Ct at 1903.

It is now beyond question that the position consistently taken by Plaintiffs/Appellants ("Plaintiffs") in this case, i.e., that the twenty-first amendment does not relieve the State of its burden of proof under the Commerce Clause to affirmatively establish that any discriminatory law actually furthers a legitimate state interest and that there is no less discriminatory alternative for accomplishing the legitimate ends of the State, is the law across the land. Here, the State has made no showing whatsoever that it is necessary or effective to give wine wholesalers resident in Michigan on September 24, 1996 who become authorized distribution agents for liquor ("ADAs"), a huge competitive advantage over non-resident ADAs who seek to become wine wholesalers. Without such a showing, just as in *Granholm*, the Michigan law challenged in this

action must also be struck down.

The State and the Association both argued to this Court that *Granholm* was wrongly decided by the U.S. Court of Appeals for the Sixth Circuit. The Supreme Court instead affirmed the decision of the Sixth Circuit in every respect. This was a gamble that Defendants lost. As a consequence, this Court should apply the precedent established by *Granholm* and declare that the statute in question is unconstitutional and void.

SUPPLEMENTAL ARGUMENT

I. SECTION 205(3) IS DISCRIMINATORY ON ITS FACE

MCL 436.1205(3) ("Section 205(3)") discriminates against out-of-state ADAs by effectively granting Michigan ADAs who are also wine wholesalers the exclusive privileges of: (1) selling the vast majority of successful wine brands; (2) "dualing" in wines; and (3) developing combined cost economies that afford the Michigan ADA/wine wholesalers an undisputed competitive advantage. Section 205(3) accomplishes this discrimination by prohibiting any ADA/wine wholesaler from "dualing"[1] with regard to any wine brands, unless the ADA/wine wholesaler was already selling that brand of wine on September 24, 1996. The facial discrimination of this statute is apparent when it is read in conjunction with MCL 436.1601 ("Section 601") which requires every wine wholesaler to have been a Michigan resident for one year prior to obtaining its wine wholesaler's license. Since Section 205(3) was enacted in December 1996, *after* the September 24 cutoff for dualing, it is impossible for any

[1] "Dualing" occurs where more than one wine wholesaler distributes a specific brand of wine in the same geographical area. Dualing is the norm for wine wholesalers who are not also ADAs. *See*, MCLA 436.1307(1) which permits and encourages competition among wine wholesalers by allowing wine suppliers to "grant the right to sell a specified brand or brands in a sales territory to more than 1 wholesaler."

non-resident ADA to obtain the advantage of dualing with regard to any wine because the only wines that can be dualed are those that were being sold prior to September 24, 1996. Since by law only Michigan residents could have been selling wines prior to September 24, 1996 (because of Section 601), Michigan residents are the only ADA/wine wholesalers who can dual. This makes it practically impossible for a non-resident ADA to catch up to the two largest resident ADA/wine wholesalers who were selling 70% of the wine brands in Michigan[2] in 1996, and who can continue to sell those brands to the exclusion of any non-resident ADA who applies to become a wine wholesaler.[3] Because of this, non-resident ADAs who wish to become wine wholesalers – such as Plaintiffs – are pretty much relegated to competing for new wines that come on the market after September 24, 1996, or unsuccessful wines that may be dropped by all other wholesalers. Given that an ADA that also wholesales wine can use the same warehouses and trucks for both wine and liquor, and deliver both to its same customers, there is no dispute that the cost economies attendant to such an arrangement give a distinct advantage to those

[2] See Mauloff Affidavit attached to application for leave to appeal as Exhibit 4. Neither the State nor the Association have submitted affidavits or other proof that Mr. Mauloff's figures are incorrect.

[3] Because there were other non-ADA wine wholesalers in business on September 24, 1996 who sold the remaining 30% of the wine brands, a non-resident ADA who applies to become a wine wholesaler is also precluded by Section 205(3) from selling any of those brands of wine, unless all other wholesalers stop selling such a brand for some reason. Thus, 100% of the wines being sold on September 24, 1996 generally cannot be sold by a non-resident ADA who applied to become a wine wholesaler.

ADA/wine wholesalers who sold wines on or before September 24, 1996.[4] By law, all of these ADA/wine wholesalers were Michigan residents. This is blatant protectionism.

The companion case to *Granholm* decided by the Supreme Court (*Swedenburg v Kelly*) is factually and legally on all fours with the case at hand. The New York law at issue in *Swedenburg* granted a preference to members of the alcoholic beverage industry that had a *physical presence* in the state, just like Section 205(3) and Section 601 grant such a preference to resident wine wholesalers in Michigan. Under the New York statutory scheme, only wineries that had a physical location in the state could obtain a license to ship wine directly to New York customers. *Granholm*, at 125 S Ct 1896-1897. This imposed a significant expense on out-of-state wineries that effectively barred them from selling directly to New York customers. *Id.* at 1897. The Supreme Court soundly criticized this particular element of the New York statutory scheme, stating, "New York's in-state presence requirement runs contrary to our admonition that States *cannot require* an out-of-state firm 'to become a resident in order to compete on equal terms.'" *Id.* (emphasis added), quoting *Halliburton Oil Well Cementing Co* v *Reily,* 373 US 64, 72; 83 S Ct 1201; 10 L Ed 2d 202 (1963). In other words, the Court was strongly suggesting that a physical presence requirement is per se constitutionally invalid.

There is no reason to distinguish between *Swedenburg* and the facts in the case at hand. Just as in *Swedenburg*, a competitive advantage was granted to Michigan resident wine

[4] There are several advantages available to the resident ADA/wine wholesalers: (1) they are able to make two deliveries (wine and liquor) from the same truck for essentially the same cost as one delivery, with a significant beneficial effect on profits, (2) they can employ the same sales people to promote both wine and liquor and (3) there are significant cost savings arising from using their work force, both laborers and administration staff, to handle both wine and liquor.

businesses that was not available to non-resident businesses, i.e., resident wine wholesalers who wished to become ADAs were given the advantage of dualing and selling thousands of brands of wines that was not available to non-resident ADAs that wished to become wine wholesalers. In fact, the Michigan law is even more onerous than the New York law. In New York a non-resident wine supplier could take up physical residence in the state and compete on the same basis as the resident wine producers. In Michigan, a non-resident ADA can *never* obtain the advantage granted to resident ADA/wholesalers because the non-resident cannot go back in time to be in a position to have brands of wines considered to be pre-September 24, 1996 wines that can be dualed. Thus, just as in *Swedenburg*, the statute conferring this benefit on State residents is discriminatory on its face.[5]

II. THE DISCRIMINATION IN FAVOR OF RESIDENT BUSINESSES VIOLATES THE COMMERCE CLAUSE BECAUSE (1) IT DOES NOT FURTHER A LEGITIMATE STATE PURPOSE AND (2) THERE ARE LESS INTRUSIVE MEANS TO ACCOMPLISH THE STATE'S STATED GOALS

The ruling of the Supreme Court in *Swedenburg* confirms what Plaintiffs argued to the trial court and the court of appeals – that conferring a benefit on Michigan residents that is

[5] Even if the Court were to determine that Section 205(3) is not discriminatory on its face, the effect of the statute is clearly discriminatory. This is admitted in the affidavit of Michael Lashbrook attached to the briefs submitted by the State as Exhibit A, and by the Association as its sole exhibit. In that affidavit, Mr. Lashbrook states in paragraph 27 that the purpose of Section 205(3) in part was "(i) to protect non-ADA wine wholesalers and the investment they made prior to the passage of the spirits privatization act; (ii) to allow wholesalers who choose to become ADAs to keep the equity they had already established in the dual brands prior to privatization of spirits, but prohibit further dualing ..." Neither of these categories could by law include an out-of-state entity because no out-of-state entity could legally wholesale wines on September 24, 1996. Thus, Mr. Lashbrook confirms what Plaintiffs have contended throughout this proceeding – that this law was intended to protect in-state businesses at the expense of out-of-state businesses. Even where a statute is not discriminatory on its face, if its effect is to discriminate against interstate commerce, it is still unconstitutional unless it survives strict scrutiny. *C & A Carbone, Inc v Town of Clarkstown, NY, 511 US 383, 389-392; 114 S Ct 1677; 128 L Ed 2d 399 (1994).* As shown below, Section 205(3) cannot survive strict scrutiny because it does not further its stated purpose of protecting the three tier wine distribution system, and there are less discriminatory measures that could accomplish the same goal more effectively.

unavailable to out-of-state businesses is discrimination that violates the Commerce Clause, unless it can pass the strict scrutiny test. In *Swedenburg*, the states offered two justifications for the discriminatory treatment of out-of-state wine producers: keeping alcohol out of the hands of minors and facilitating tax collections by the state. The Court considered each rationale and rejected them for essentially three reasons: (1) the states had presented little evidence to support their claims, (2) the discriminatory law did not actually accomplish the goals announced by the states as the reason for the law and (3) there were less discriminatory alternatives available that would accomplish what the states were trying to do. *Id.* at 1905-1906. Plaintiffs presented these same arguments in their application for leave to appeal on pages 28-31, and would refer the Court to those pages to be considered in light of the confirming reasoning enunciated by the U.S. Supreme Court in *Granholm.*

There is another analogy to be drawn between *Granholm* and the case at hand. In both cases judgment was entered on cross-motions for summary disposition/judgment. *Id.* at 1894. In both cases, the parties relied on affidavits to support their claims. *Heald v Engler (Granholm),* 342 F3d 517, 520 (CA6, 2003). The Supreme Court stated:

> In summary, the States provide little concrete evidence for the sweeping assertion that they cannot police direct shipments by out-of-state wineries. Our Commerce Clause cases demand more than mere speculation to support discrimination against out-of-state goods. The "burden is on the State to show that 'the *discrimination* is demonstrably justified... '" (cites omitted). The Court has upheld state regulations that discriminate against interstate commerce only after finding, based on concrete record evidence, that a State's nondiscriminatory alternatives will prove unworkable. (cites omitted). Michigan and New York have not satisfied this exacting standard.

Granholm at 125 S Ct 1907. This Court should conclude that Michigan has once again not satisfied this "exacting" standard. Just as in *Granholm*, the state here has presented little in the way of concrete evidence that supports its claim that Section 205(3) was necessary to protect the middle tier of the wine distribution system. The affidavits presented actually support Plaintiffs' position that the statute is discriminatory, while at the same time offering no evidence, nor logic, beyond mere speculation, that establishes that this statute either protects the stability of the system or that the stability of the system could be protected, if necessary, by less discriminatory legislation.[6] See Plaintiffs' application for leave to appeal, pp. 28-31 for a complete discussion of this argument. If such evidence existed, the State could have presented it in support of its motion for summary disposition. The absence of such proof is fatal to the Defendants' case, just as it was in *Granholm.*

III. THE TWENTY-FIRST AMENDMENT DOES NOT SAVE SECTION 205(3)

As noted above, the State and the Association have argued throughout this case that, even if Section 205(3) otherwise violates the Commerce Clause of the U.S. Constitution, the twenty-first amendment to the Constitution saves this statute from being declared unconstitutional. When the U.S. Court of Appeals for the Sixth Circuit rejected this same argument made by the State and the Association in the *Granholm* case, the State and the Association declared to this Court that the Sixth Circuit was wrong. Of course, it was the Sixth Circuit and Plaintiffs here that were vindicated when the Supreme Court issued its decision in *Granholm*. It is now absolutely clear that everywhere in the United States, the Commerce Clause must be given its

[6] In the final analysis, Section 205(3) actually works against the states' interest because it discourages other non-resident ADAs from competing in this state.

due, even in the arena of alcoholic beverage regulation by states. When the Commerce Clause test is applied to the facts in this case, as shown above and in Plaintiffs' application for leave to appeal, there can be no dispute that the September 24, 1996 date in Section 205(3) targeted the Plaintiffs and other non-resident ADAs, and that it cannot survive strict scrutiny. The twenty-first amendment does not and cannot save this discriminatory statute.

IV. PEREMPTORY RELIEF IS APPROPRIATE

In light of *Granholm* which has already declared that a significant section of the Michigan Liquor Code is unconstitutional, there is no reason to delay this Court's determination that Section 205(3) is likewise unconstitutional. The parties have presented all the arguments and record evidence with their briefs in support of and in opposition to this application for leave to appeal that are relevant to the Court's determination. This Court has all the information it needs to find, consistent with *Granholm*, that Section 205(3) violates the Commerce Clause and is not saved by the twenty-first amendment. There is no reason it cannot take action peremptorily under these circumstances.

For these reasons, Plaintiffs respectfully ask this Court to grant their application for leave to appeal and to strike down MCL 436.1205(3) as unconstitutional.

Respectfully submitted,

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